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SUBJECT: IMF ASSESSMENT OF TAJIK ECONOMY AND REFORMS: CAUTIOUSLY  
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11. (SBU) Summary: An IMF team recently completed a two-week visit to Dushanbe to assess economic and government performance before releasing a second tranche of funding under the Poverty Reduction and Growth Facility (PRGF). Briefing donors, the team noted the Tajik government had met most of its structural and quantitative targets. The government agreed to publicly release audits of key state-owned enterprises, including the electrical operator Barqi Tojik and the Talco aluminum company. Long-overdue annual audits of the National Bank -- a formal requirement for release of the PRGF funding -- should soon be underway. The IMF noted that Tajikistan's economy was doing "surprisingly" well given the world economic crisis, and was expected to grow by 2-3% this year. Modest growth is predicted for next year. Inflation remains low, at just 4%. The government's single major failure has been the 35 million somoni in pension arrears it has run. The President has committed to paying these off by November, although by what means remains unclear. The IMF continues to recommend that the National Bank allow a controlled devaluation of the somoni to boost exports and improve the lopsided trade balance. The IMF is keeping an eye on government debt, although this is expected to rise next year. End summary.

GOVERNMENT AGREES TO RELEASE KEY AUDITS

12. (U) A team from the International Monetary Fund (IMF) just completed a two-week visit to Dushanbe to assess Tajikistan's macroeconomic conditions and progress on structural reforms. The assessment, intended to measure progress over the first half of 2009, is a prerequisite for disbursing a second tranche of approximately \$28 million under the IMF's Poverty Reduction and Growth Facility (PRGF). A first tranche of \$40 million was disbursed in April; the IMF will deliver a total of \$116 million over three years. During a September 24 breakfast meeting with Ambassador and Econoff and at a briefing for donors later in the day, Washington-based IMF mission chief for Tajikistan Axel Schimmelpfennig and Resident Representative in Tajikistan Luc Moers were cautiously optimistic about the government's progress in making key structural reforms and the country's resilience in the face of the global economic crisis.

13. (SBU) Schimmelpfennig announced that the government had just that afternoon agreed to release an audit of the state-owned electrical grid operator, Barqi Tojik, completed earlier this year. (Note: Secretary Clinton brought this issue up with President Rahmon on the margins of UNGA, noting that releasing the audit would be an important indication of Tajikistan's genuine desire for economic reform. As late as the morning of the IMF briefing, the government was still declining to release the audit. No publication date for the audit has been announced. End note.) Schimmelpfennig said that several years of annual audits of the state-owned Talco aluminum plant would be published on the company's website by December or January. The audit of 2005 is almost done, and the British accountancy firm Moore Stephens will soon be turning to 2006 to 2008.

14. (SBU) After a series of fits and starts, it appears that long-overdue annual audits of the National Bank will now get underway. The last signed audit of the Bank was for the year 2005 by PriceWaterhouseCoopers. Audits of two successive years were unsigned, apparently because of major discrepancies in the Bank's accounts (ref B). Schimmelpfennig said that in all likelihood KPMG would conduct the new audit, which would cover fiscal year 2008, ending in April 2009 (the Bank is currently working to align its fiscal year to the calendar year). Completion of this audit is a formal requirement for the disbursement of the second tranche of IMF funding, which had initially been expected to occur within the next month or two. KPMG had a team in Dushanbe two weeks ago doing a due-diligence survey, or "pre-audit." Schimmelpfennig told the Ambassador privately that the pre-audit team, based out of Almaty, was recommending that KPMG take on the project, but would have to

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push to convince office principals that the firm should run the risk. Given the audit delays, the IMF was unlikely to release the second tranche of funding before January 2010. If things are further delayed, the Fund would combine the second tranche with its next mission, currently scheduled for February 2010, to assess end-2009 performance data. Schimmelpfennig said that in view of better-than-expected economic growth, the delay would not pose any risk to the budget, and he was fairly optimistic that the audit would soon be underway.

15. (SBU) The government passed a cotton debt resolution plan in July, although implementation would be a challenge (ref A). The government has already asked the IMF for technical assistance with the project, and the IMF has someone looking at the issue. In the earlier breakfast meeting with the Ambassador, Schimmelpfennig and Moers admitted that the IMF did not have much information about the cotton reform process and was consequently relying on the donor community for information and assistance in ensuring that the project was implemented properly.

SOME TARGETS MET; OTHERS NOT SO MUCH

16. (U) According to the IMF assessment team, the Tajik government has met most of the quantitative targets set out for it by the IMF. The one clear exception has been the approximately 35 million somoni (\$7.9 million) in pension arrears that the government owes. Schimmelpfennig said, however, that he had a firm commitment from President Rahmon to make all back pension payments by November. When asked later in the briefing where that money would come from, given the government's already strained budget, Schimmelpfennig admitted he did not know. He said that the IMF might advise the

government to close some tax loopholes and lift the value-added tax (VAT) back to 20%, after having been lowered to 18% earlier this year. The government appeared to have fallen just short of the IMF-mandated target for social sector spending, but Schimmelpfennig said the difference is so small -- just 4 or 5 million somoni (approximately \$1 million) -- that it "lies within the margin of error." Most importantly, he said, social spending picked up significantly in the second quarter after being slack through Q1.

17. (SBU) European Community Charge d'Affaires Charlotte Adriaen noted that she and others in the room had heard a good deal of anecdotal evidence that the government was also running significant wage arrears. She said contacts in Sughd province had reported that even teachers and health workers, whose salaries should be protected under the minimum social sector spending targets, were not receiving their wages. Schimmelpfennig said the government had admitted to some "minor technical delays" in wage payments but reported that most salaries were being paid on time. The IMF team acknowledged that the government might be understating the issue, but said the Fund, absent any systematic data to the contrary, had to accept the government's figures.

#### SURPRISING GROWTH IN TAJIK ECONOMY

18. (U) The IMF team reported that the Tajik economy was performing surprisingly well considering the global financial crisis. GDP growth for the year was expected to reach 2-3%, in the face of a 1% decline worldwide and a 7.5% drop in Russia, to which Tajikistan's economy is closely linked. Schimmelpfennig credited the economic growth to the relatively robust performance of the non-cotton agricultural sector, which was helped by abundant spring rains. The government of Tajikistan was forecasting GDP growth of 5% for 2010, which the IMF believed was reasonable. The IMF is predicting that the world economy will expand by 3%, fueled mainly by growth in China and

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emerging markets. Russia's GDP is expected to increase modestly by 1.5% in 2010. Schimmelpfennig said that IMF's projections were perhaps slightly optimistic compared to others.

19. (U) Remittances from Tajiks working abroad, chiefly in Russia, are still some 30% below 2008's record levels. The IMF team predicted that next year will see a modest turnaround, with levels rising by 5%. Making accurate predictions is difficult, however, because it depended on the dollar-ruble exchange rate. In a positive sign, inflation had been low this year, reaching just 4% this August, year-on-year. The IMF predicts that it will increase to as high as 8% by the end of this year and 11% by end-2010, averaging 9.0-9.5% for the year.

#### IMF ADVICE FOR TAJIK GOVERNMENT

110. (U) The IMF believes that despite earlier devaluation of the Tajik somoni from around 3.4 to the dollar in late 2008 to 4.4 to the dollar today, Tajikistan's currency remains overvalued and should be allowed to further depreciate in real terms. This will help relieve the high trade deficit by creating more opportunities for Tajik exports. As they noted in previous visits, the IMF team said the National Bank's key role should be to ensure that the devaluation is smooth. The Bank lacked the currency reserves to significantly affect the somoni exchange

rate and consequently should not try to do anything more than even out the rough patches.

¶11. (SBU) The IMF has agreed with the government to increase the recommended budget deficit to 1% of GDP in 2010 from 0.5% of GDP this year. The government said it needed the increase to raise wages and pensions next year. Total government debt this year is not to exceed 40% of GDP (this excludes recapitalization of the National Bank, which may increase the figure by 10-12%). Schimmelpfennig said the government was looking at debt of 46% of GDP in 2010 (again without bank recapitalization), which might be a bit high. He said the Fund would be watching state borrowing carefully. China has discussed lending a total of \$10 billion to Shanghai Treaty Organization countries, although it is unclear how this might be divided among the ten member states. Schimmelpfennig said that if China decided, for example, to offer \$1 billion to Tajikistan, this would equal one-half of current debt. "We would certainly have concerns about debt sustainability if that happened." He noted, however, that the Chinese Ambassador to Tajikistan had told him earlier in the week that China had not made any determination to offer the loans, and had made no decisions about how much might be offered to each country if any loans were made.

¶12. (SBU) Comment: The government appears to have taken some genuine steps to increase economic performance and the investment climate in recent months, including new laws easing business registrations, more transparent banking rules, and a major overhaul of the agricultural sector. The announcement that the Barqi Tojik audit will be released comes as further welcome news. Whether these steps represent a cynical effort to curry favor with the donor community to help weather the financial crisis or a deeper desire to reform remains to be seen. Either way, the IMF appears to be playing a more constructive role. While a year ago donors were visibly shaking their heads at the Fund's overly rosy economic projections and assessments of government performance, IMF team members are now more critical in their appraisals. And the government may be taking notice. End comment.  
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